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MONTANA CHILDRENS' CENTER

REPORT ON EXAMINATION

Fiscal Year Ended June 30, 1967

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MONTANA CHILDRENS' CENTER

REPORT ON EXAMINATION

Fiscal Year Ended June 30, 1967

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APPOINTIVE AND ADMINISTRATIVE OFFICIALS

Board of Institutions

H. T. Caraway, M.D., Chairman	Billings	July, 1968
Henry Loble	Helena	July, 1969
John M. Cross	Glendive	July, 1970
Ella Mae Cromer	Butte	July, 1971
Arthur Hoff	Lewistown	July, 1972

Department of Institutions

Edwin G. Kellner	Director

Montana Childrens' Center

Joseph M. Balkovatz	Superintendent

SUMMARY OF RECOMMENDATIONS

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Establish a general journal for recording adjusting, closing, and other infrequent transactions.	4
Prepare reports of collections and reassign responsibilities for handling cash receipts to improve controls.	5
Record reports of collections daily and deposit monies at least weekly.	6
Prepare journal records showing the date the safe combination was last changed and the names of the persons knowing the combination. Establish policy to change combination whenever a person's responsibility no longer requires his knowledge of the combination.	6
Establish safeguards over the custody of blank check stock and the keys to operate the check protector.	7
Set up contingent revolving fund on an imprest basis with only two entries in the accounting records.	8
Maintain a revolving fund cash book for the recording of revolving fund transactions exclusively. Establish a revolving fund receivables ledger to record unreimbursed expenditures from the fund.	9
Adjust revolving fund cash account at year-end to properly reflect the assets represented.	10
Require agencies to submit substantiating invoices in support of revolving fund reimbursement claims.	10
Prepare required financial statements on a fund basis consistent with generally accepted governmental accounting principles.	11
Finalize the formalization of employee leave records, update monthly records of employees using leave credits, consider preparing and distributing annual statements of leave credits.	12
Prepare officially approved employee attendance reports and retain them as support for salary payments made.	12
Send notice to each agency affected by accounting entries initiated by a control agency.	13

SUMMARY OF RECOMMENDATIONS (Continued)

	Page
Account for and report separately operations of separate programs within a fund.	14
Record changes in fixed assets in the year in which they occur. Adjust land account records to reflect 1961 sale.	14
Record fixed assets at cost in accordance with generally accepted governmental accounting principles.	15
Record construction expenditures on incomplete projects in fixed assets as construction-in-progress pending their completion.	15
Account separately for costs applicable to separate appropriations.	16
Establish and maintain on a current basis detail ledgers in support of fixed asset control accounts.	17
Complete installation of a system for identifying and controlling equipment items.	17
Require superintendent's approval for all write-offs of fixed assets.	17
Expand Reserve for Investment in General Fixed Assets account to reflect source of financing for asset acquisitions.	18
Adhere to the present requirements of law that establish the purposes for which specific appropriations can be expended.	20
Adopt the modified accrual basis of accounting for all state agencies in order to properly account for expenditures and avoid overexpenditure of appropriations.	22
Re-evaluate and improve controls over appropriation accounting.	23
Initiate a plan to assure compliance with Budget Act provisions regarding purchases of subsequent year goods and services from current year appropriations.	24
Establish procedures to control and document equipment purchases to assure compliance with Budget Act provisions.	26

MORRIS L. BRUSETT, C.P.A.
LEGISLATIVE AUDITOR

G. DEAN REED, C.P.A.
DEPUTY

STATE OF MONTANA

Office of the Legislative Auditor

STATE CAPITOL
HELENA

The Legislative Audit Committee
of the Montana State Legislature:

We have examined the balance sheets of the General Fund, Federal and Private Revenue Fund, Bond Proceeds and Insurance Clearance Fund, Agency Fund, and the General Fixed Assets Account of the Montana Childrens' Center as of June 30, 1967, and the related Statements of Changes in Fund Balance and Expenditures and Encumbrances Compared with Appropriations for the year then ended. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The financial statements have been prepared on the cash basis of accounting and do not show financial position or operating results as do statements prepared on the modified accrual basis in accordance with generally accepted accounting principles applicable to governmental units.

The buildings are shown in the General Fixed Assets Account at the assigned insurance value rather than on the basis of original cost. Original cost is the generally accepted method used for valuing fixed assets for reporting purposes. The assigned insurance value exceeded the original cost by $688,000.

Certain legal provisions, regarding the expenditure of Legislative appropriations, have not, in accordance with generally accepted governmental accounting principles, been adhered to as outlined in the comments section of this report.

In our opinion, subject to the exceptions described in the preceding paragraphs, the accompanying financial statements, except for the General Fixed Assets Account group, present fairly the financial position of the General Fund, Federal and Private Revenue Fund, Bond Proceeds and Insurance Clearance Fund, and Agency Fund of the Montana Childrens' Center as of June 30, 1967, and the results of its operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

However, because buildings are shown at a value that exceeds cost by $688,000, we are unable to express an opinion that the balance sheet of the General Fixed Asset Account group presents fairly the financial position of that group of accounts.

We submit the financial statements listed in the preceding table of contents together with the following comments.

COMMENTS

GENERAL

The Montana Childrens' Center, located on approximately 215 acres adjacent to the town of Twin Bridges, was established in 1893. Children, through age sixteen, are admitted to the Center through the district courts. The Center provides these children with support and care as well as educational facilities.

The investment of the State in the facility, exclusive of equipment, is approximately one million dollars. The institution retains a staff of approximately 60 employees. $480,738 was expended from the General Fund towards the support of the institution in 1966-67 fiscal year. The average daily cost per child for the year as computed by the Childrens' Center, was $9.48.

The Childrens' Center operates under the general supervision of the Department of Public Institutions. The Department of Public Institutions is guided by policies established by the Board of Institutions, which consists of five members appointed for five year terms by the Governor subject to confirmation by the Senate.

BOOKS OF ORIGINAL ENTRY

Books of original entry usually consist of registers and a general journal. Registers are special journals designed to provide separate chronological records of the different types of transactions of more than one fund provided such arrangement facilitates bookkeeping. The appropriate journal entry or entries required to summarize transactions recorded each month in each register will usually be written in the register in the space

beneath the totals footings for that month. These end-of-month entries will then be posted to the ledgers. Therefore, a general journal should be used solely for recording adjusting entries, closing entries, and other transactions occuring too infrequently to justify establishing a register.

The Childrens' Center maintains various registers, i.e. cash receipts, cash disbursements, voucher journal, etc. However it does not maintain a general journal. Instead it uses the voucher journal (claims filed register) as the book of original entry for recording not only claims filed with the State Controller but also adjusting, closing and other infrequent entries. The Center, in order to maintain proper numerical sequence in the register, must assign a claim number to every entry recorded regardless if the entry is supported by a claim or by a journal voucher. The comingling of dissimilar entries within the one register results in an unorthodox and cumbersome bookkeeping system.

RECOMMENDATION

We recommend that a general journal be established as the book of original entry for recording adjusting, closing, and other transactions which occur infrequently.

INTERNAL CONTROL OVER CASH TRANSACTIONS

Ideally the system of internal control over cash transactions should provide assurance that (1) all cash which should have been received was in fact received and recorded promptly and accurately, (2) cash disbursements have been made only for authorized purposes and have been properly recorded, and (3) cash on hand and in bank is accurately stated and subject to appropriate safeguards.

In our review of the system of internal control over cash transactions, we found certain weaknesses which we believe should be corrected. In an

agency such as the Childrens' Center which has only a small office staff, it is often difficult to obtain the proper segregation of duties among the available personnel. However, the implementation of our recommendations, which follow, should provide an effective system of internal control over cash transactions without adding new personnel to the present office staff.

Findings and recommendations:

1. Proper accountability for cash has not been established at the initial point of receipt. Formalized reports of collections should be prepared by the personnel responsible for opening the mail. In addition, a further segregation of duties should be made so that a single individual is not responsible for receiving cash as well as having control over the accounting records relating thereto. We suggest that the duties relative to cash be reassigned as follows:

Employee	Duties
Houseparent supervisor	Open childrens' mail, prepare report of collections in duplicate.
Superintendent's secretary	Open other mail, prepare report of collections in duplicate.
Assistant Accountant	Receive money and original copy of reports of collections, post cash receipts register, prepare bank deposit slip in duplicate.
Superintendent (or Business Manager)	Receive duplicate copies of reports of collections and bank deposit slips, compare on test basis, retain for audit.
Accountant	Post to general ledger, reconcile bank account.

RECOMMENDATION

We recommend that reports of collections be prepared at the initial point of the receipt of cash and that the duties relative to cash be reassigned in accordance with the chart that is illustrated in the preceding paragraph.

2. Cash receipts are not always recorded daily as is recommended. Cash, representing collections other than contingent fund reimbursements and other relatively large amounts, is not deposited in the bank until the end of the month. Undeposited collections accumulated during a month have varied in amounts from month to month with a high of approximately $3600.

RECOMMENDATION

We recommend that receipts and reports of collections be recorded daily in the accounting records and that bank deposits be made at least weekly and more frequently if necessary to avoid a large accumulation of cash.

3. The Center does not keep a record showing the date the safe combination was last changed and the names of the employees that have knowledge of the combination. The combination to the safe has not been changed for several years even though several employees who knew the safe combination have since left the employment of the institution.

RECOMMENDATION

We recommend that a journal record be kept showing the date the safe combination was last changed and the names of the persons knowing the combination and that a policy be initiated whereby the combination will be changed whenever the responsibility for the contents of the safe is no longer appropriate to a person having knowledge of the combination.

4. The agency keeps on hand a stock of blank checks for use in writing checks on the contingent fund and the childrens' trust accounts. The Center also employs the use of a check protector which is used to imprint the proper

amounts on the face of the checks. However, the blank check stock is left in an unlocked vault overnight and the key to the check protector is left in the equipment overnight. This situation enhances the possibility of misuse of the checks and the check protector.

RECOMMENDATION

We recommend that the blank check stock be placed in a locked safe when not being used and that the key to the check protector be removed from the equipment overnight and similar measures provided for its security.

CONTINGENT REVOLVING FUND

Section 79-602, R.C.M. 1947 gives the State Controller the authority to establish, under specific regulations, contingent revolving funds at state agencies. The statute further states that each state institution granted a contingent revolving fund shall report to the State Controller monthly all transactions involving such contingent revolving accounts, with proper vouchers for every payment made therefrom. The State Controller may cancel such authorizations and recall such funds at his pleasure.

We believe that throughout the fiscal year contingent fund cash should be accounted for on an imprest system. An imprest system is used for handling payments that will be made directly by the agency from a fixed amount of money, designated as revolving fund cash, advanced to the agency for this purpose. Disbursements are made as needed, with a receipt or petty cash voucher being completed in each case. At certain intervals, or when the revolving fund cash is nearly exhausted, a claim with substantiating invoices is prepared and the revolving fund cash account is replenished for the amount of disbursement by a warrant drawn on the State Treasury against the

proper appropriation. The total of revolving fund cash on hand plus the amount of signed receipts or invoices paid at any one time must equal the total amount of revolving fund cash authorized.

The 34th Legislative Assembly advanced $2,500 from the General Fund to the Childrens' Center to be used as a revolving fund. During our review of the procedures and accounting practices regarding the contingent revolving account, we noted some deficiencies in the present system which should be corrected. These are listed below together with our recommendations.

(1) Although the Balance Sheet, Exhibit A, has been adjusted to correctly present the accounts, the contingent fund as accounted for by the agency is shown twice as an asset and twice as a reserve as follows:

Acct #612	Cash in Bank	$1,456	
Acct #73	Contingent Fund		$1,942
and also -			
Acct #610	Advance from State Treasurer	2,500	
Acct #76	Advance by State Treasurer		2,500

The first set of accounts is used to reflect all transactions affecting the contingent fund; balances are reduced and increased as checks are written and reimbursements received. The cash account, obviously, is not on an imprest basis.

The second set of accounts has been set up as contra accounts. Accounting transactions are not posted to these accounts.

RECOMMENDATION

We recommend that the revolving fund cash account be set up on an imprest basis and that only the following two accounts be maintained

on the accounting records:

Revolving Fund Cash	$2,500	
Revolving Fund Advance		$2,500

(2) Under the current system revolving fund cash transactions are recorded in the regular cash receipts register; and a formal subsidiary record of revolving fund expenditures, which are pending reimbursement, is not maintained. The separation of the accounting for revolving fund cash from other cash accounting would provide a greater degree of control and an exact accountability at any time of the amount advanced.

RECOMMENDATION

We recommend that a revolving fund cash book be established in which all and only revolving fund transactions would be recorded and that a revolving fund receivables ledger be established in which would be recorded, by descriptive type, expenditures made but not yet reimbursed. At any one time the total of the amounts in the receivables ledger and in the cash book would be equal to the amount authorized for revolving fund purposes.

(3) To the extent that such revolving funds consist of items other than cash, the imprest basis has the effect of overstating cash in the agency's statements. Therefore appropriate adjusting entries need to be made in the general ledger as of June 30 to the accounts of each fund affected. These adjustments will reduce, for year-end statement purposes, the balance of the revolving fund cash account to the adjusted cash book balance of the revolving fund, and set up on the financial statements the assets represented by the net cash outlay at year-end such as deferred charges, due from other funds, etc.

RECOMMENDATION

We recommend that the revolving fund cash account be adjusted at year-end to properly reflect the nature of the asset.

(4) As stated above, the statutes state that agencies with revolving fund advances shall report to the State Controller monthly all transactions involving such contingent revolving accounts, with proper vouchers for every payment made therefrom.

Presently, most of the agencies submit with their revolving fund claim for reimbursement a listing of the checks written showing payee, purpose, and amount paid. A few agencies submit with their claims substantiating invoices for which the revolving fund checks were written. The submission of the supporting invoice with the claim allows the Controller to make a meaningful pre-audit (as with regular claims) as well as enabling him to determine if the revolving fund is being used in accordance with his prescribed procedures.

RECOMMENDATION

We recommend that the State Controller require all agencies to submit the appropriate invoices, supporting revolving cash payments, with their revolving fund reimbursement claims.

FINANCIAL REPORTING

The diverse nature of governmental operations and the necessity of determining legal compliance preclude a single, unified set of accounts for recording and summarizing all of the financial transactions of a governmental unit. Instead the required accounts are organized on the basis of funds, each of which is completely independent of any other. Each fund must be so accounted for

that the identity of its resources, obligations, revenues, expenditures, and fund equities is continually maintained. These purposes are accomplished by providing a complete self-balancing set of accounts for each fund which show its assets, liabilities, reserves, fund balances, revenues, and expenditures. The financial statements and schedules should be prepared directly and exclusively from the accounts and should include, for adequate reporting of governmental finances, balance sheets, operating statements, and final budget reports on an individual basis.

The Childrens' Center prepared pre-closing and post-closing combined funds trial balances as of June 30, 1967. We felt it necessary, for adequate disclosure of the financial position and results of operations of the institution, to construct for this report the required financial statements on an individual fund basis (See Exhibits).

RECOMMENDATION

We recommend that the required financial statements be prepared by the agency on a fund basis in accordance with generally accepted governmental accounting principles.

PAYROLL

The Childrens' Center is currently in the process of formalizing "Employee Leave Records" and accumulating vacation balances for posting to the new records being established. We are in agreement with the agency that their leave records should be formalized and also suggest that: (1) each month, the records of employees who have used leave credits during the current month be updated - only at that time does the balance available need to be known. (2) since current laws prohibit employees from carrying over to a calendar year more than thirty days accumulated vacation, it would be

beneficial to an employee if an annual statement of leave credits was prepared and distributed sometime around October 1 of each year.

RECOMMENDATION

We recommend that the formalization of employee leave records be finalized; that each month the records of the employees who have used leave credits during the current month be updated; and, that consideration be given to preparing and distributing annual statements showing leave credits.

Employee time sheets are prepared by the various supervisors in pencil and then forwarded to the accounting office at the end of each month. After the accounting office has completed processing the time reports, they are returned to the respective unit supervisors. Although the time records are supposed to be prepared and approved by the supervisors, the supervisors do not indicate by a certifying signature that they have approved the report.

RECOMMENDATION

We recommend that employee attendance reports be prepared in ink, signed by the proper official, and retained in the accounting office as supporting documentation for salary payments made.

CONTROL AGENCIES' ACCOUNTING

1. Certain accounting transactions that effect the Childrens' Center accounts are now being recorded by the central control agencies without a notification being sent to the Center that such transactions have taken place. In particular, we are referring to interest that was earned on agency accounts for monies held in the State Treasury and then distributed to the Center's account. Since the Center was not notified of the interest

distribution, the first indication they had of this distribution was when they received the next monthly Controller's report and found that they were unable to balance their records with those of the Controller because of the unidentified, and on the agency's part unrecorded, collection representing the interest distribution. In order to avoid similar problems each agency that is affected by an accounting entry initiated by another agency should receive a copy of the document supporting such entry.

RECOMMENDATION

We recommend that each agency that is affected by an accounting entry initiated by a control agency be sent a copy of the document supporting such entry.

2. Included in the Controller's account #410524 of the Federal and Private Revenue Fund are two different types of revenue, each one of which has distinct restrictions as to the use for which the funds can be applied. The two programs whose funds were comingled within the one account are:

(1) Special Milk Program - these funds represent monies received from the federal government for and restricted to the purchase of milk and/or supplies and equipment that promote the consumption of milk.

(2) Private bequest available for and restricted to Center construction purposes.

Although the agency accounts for the two programs separately, we believe the Controller, who is responsible for pre-auditing claims to determine that they are charged to the proper fund and that they are not illegal, should also account for the programs separately so as to minimize the possibility that funds restricted to one program will not be improperly expended thus creating

a liability against the State.

RECOMMENDATION

We recommend that the operations of separate programs within the Federal and Private Revenue Fund be accounted for and reported separately by the State Controller.

GENERAL FIXED ASSETS

Exhibit G of the financial statements presents a statement of changes in the general fixed assets of the Montana Childrens' Center for the fiscal year ended June 30, 1967 as they were accounted for by the agency.

Overstatement of Reported Amounts

As shown by the statement, additions and deletions of equipment items for the preceding year were not recorded until 1966-67. Additions for 1966-67 were properly recorded during the year, however, write-offs totaling $1,912 applicable to 1966-67 were not recorded until 1967-68. The equipment balance is accordingly overstated $1,912 at June 30, 1967.

The recorded land balance of $4,271 is overstated $1,118 due to the incorrect recording of the sale of 12.77 acres of land sold in 1961. The cost of the land sold was not removed from the land account balance and in addition, the sales price was added to the land balance in error.

RECOMMENDATION

We recommend that:

(1) Fixed asset accounting procedures be revised to record applicable additions and deletions in the year-end financial reports.

(2) The land account be adjusted to properly reflect the 1961 sale of 12.77 acres.

Recorded Value of Buildings

The $1,688,019 balance of the buildings account represents the insurance value of the buildings as of December 1961. The latest insurance value computed was $1,488,700 as of July 1965. One of the basic principles of governmental accounting is that fixed assets be recorded at cost. Recording the fixed assets at cost will result in their recorded value corresponding to the expenditure accounts from which they were financed. Cost valuation ordinarily can be readily determined from source documents involved in the acquisition transaction. Cost valuation remains stable and is not subject to change at such times as when it is determined that the agency's insurance should be re-evaluated.

RECOMMENDATION

We recommend that fixed assets be recorded at cost in accordance with generally accepted governmental accounting principles.

Unrecorded Construction Work-In-Progress

During 1966-67, construction expenditures totaling $108,244 were incurred which are not reflected in the fixed asset group of accounts at June 30, 1967. The agency's statements are understated and incomplete with these project costs omitted. Such costs should be capitalized as construction-in-progress until the projects are completed at which time they would be transferred to the applicable completed asset account.

RECOMMENDATION

We recommend that a system be initiated whereby construction expenditures on incomplete projects will be recorded in fixed assets as construction-in-progress pending their completion.

Comingling of Appropriated Projects Costs

As shown by Exhibit E, the Childrens' Center appropriations for 1966-67 included a $7,000 separate appropriation for the repair of the Center's water tank. This repair work was included in the contract let for the agency's appropriation for the repair, renovation, reroofing of cottages and gymnazium and providing a new water supply system. This was the most economical means of having the water tank repaired and we concur with this approach. However, the costs of the separate projects were not accounted for separately. As accounted for by the agency and State Controller, only $350 was expended on the water tank repair. Exhibit E presents the actual costs of $5,751. All costs for each appropriation should be accounted for separately in order to maintain proper appropriation control and fixed asset records.

RECOMMENDATION

We recommend that all costs applicable to an appropriation be accounted for separately as opposed to being comingled with those of another appropriation.

Control of Fixed Assets

The Childrens' Center does not maintain a detail ledger supporting their control accounts for land, buildings, and improvements. Department of Institutions directives provide that such a detail ledger be maintained and we concur. A detail ledger would provide a description, location, cost, source of financing, and other pertinent information relating to the individual assets comprising the reported totals. Such a ledger would provide the agency with a good working tool for management and control of its land, buildings, and improvements as it presently has for its equipment items.

The agency's equipment items are not marked with identification numbers.

Equipment records presently are being maintained by description and location only. This lack of identifying numbers causes difficulties in taking physical inventories with resulting lack of control. The agency has initiated plans to start marking its equipment items.

Equipment items written off for 1966-67 by the agency did not have the written approval of the Center's superintendent. In order to maintain adequate control of its equipment, write-offs of the Center's equipment should be approved in writing by a responsible agency official.

RECOMMENDATION

We recommend that:

(1) A detail ledger be established and maintained on a current basis in support of the Childrens' Center control accounts for land, buildings, and improvements.

(2) The agency complete its plans for marking and controlling its equipment items by identifying numbers, implement the plans, and maintain this system on a current basis.

(3) Write-offs of the institution's fixed assets be approved in writing by a responsible agency official.

Source of Financing

In order to present a statement of general fixed assets that makes adequate disclosure as to the nature, cost, and source of the agency's fixed assets, the accounts should disclose the source of financing of the assets. For example, the account shown on the Balance Sheet, Exhibit A, as Reserve for Investments in General Fixed Assets totaling $2,047,449 would be broken

down into sub-accounts reflecting the source of financing similar to the following:

Bond Proceeds

Federal Grants

General Fund Appropriations

Gifts

Provision for such a presentation is included in Department of Institutions directives. We concur that such a presentation would result in a more meaningful financial disclosure of the agency's fixed assets.

RECOMMENDATION

We recommend that the Childrens' Center expand their Reserve for Investment in General Fixed Assets to account for their fixed assets by source of financing.

CONTROLS OVER APPROPRIATIONS

One of our objectives, as set forth by law, in our examination of the Childrens' Center was to determine that expenditures were made only in furtherance of authorized activities and in accordance with the requirements of applicable laws and regulations.

Our findings and comments related thereto follow.

Expenditure of Operating Funds for Capital Construction

The 1965 Legislature appropriated from the long-range building program account in the Bond Proceeds and Insurance Clearance Fund $192,000 for capital projects at the Childrens' Center.

Following we show in schedule form (1) a recap of expenditures and source of funds and (2) a recap of the approved contract expenditures.

(1) Recap of Expenditures and Source of Funds

	Bond Proceeds and Clearance Fund	Federal and Private Revenue Fund	General Fund	Total
Expenditures				
1965-66 F.Y.	$ 40,259	$ -	$ -	$ 40,259
1966-67 F.Y.	108,244	-	-	108,244
1967-68 F.Y. (to 3-1-68)	43,417	8,261	491	52,169
Total Expended	191,920	8,261	491	200,672
Balance due contractors (known)	80	920	-	1,000
Total Expended and Estimated Balance Due	$192,000	$9,181	$491	$201,672
Source of Funds				
1965-67 Appropriation:				
New Boiler	$ 55,000	$ -	$ -	$ 55,000
Repair and Renovate Buildings and New Water Supply System	130,000	-	-	130,000
Repair Water Tank	7,000	-	-	7,000
Agency Bequests:				
Offerdahl-principal	-	6,219	-	6,219
Offerdahl-interest	-	1,009	-	1,009
Zeuchner-principal	-	1,953	-	1,953
1967-69 Appropriation:				
Operation and Capital	-	-	491	491
Total	$192,000	$9,181	$491	$201,672

(2) Recap of Approved Contract Expenditures

Original Contracts Let	$193,293
Change Orders Approved	7,830
Additional Miscellaneous Expenditures	549
Total	$201,672

House Bill No. 535, Budget Act of 1965, Section 3, states "There is also appropriated to the Department of Institutions all monies from federal, or private or other sources which may be available to finance the capital projects included in this act." In the foregoing section the Legislature has granted permission to use the $9,181 expended from the Federal and Private Revenue Fund.

However, Extraordinary Session House Bill No. 9, Budget Act of 1967, Sections 3 and 4 clearly state that the appropriation from the General Fund for operation and capital for the 1967-69 biennium shall not be expended for capital projects including the construction, improvement, betterment, or furnishing of buildings, structures, or purchase of buildings or land unless specifically authorized.

In this particular instance the State Controller approved the expenditure of $491 from the Childrens' Center 1967-68 Fiscal year General Fund operation and capital appropriation as partial payment of consulting engineers' fees associated with one of the capital construction projects.

Although the $491 represents a rather insignificant amount of money (we have at this time no way of knowing how material comparable amounts may be in regards to other agencies), it is clearly stated in the Budget Act that funds appropriated for operations and capital shall not be used for major capital construction projects and the disbursement was made contrary thereto.

RECOMMENDATION

We recommend that the State Controller adhere to the present requirements of law which establish the purposes for which specific appropriations can be expended.

Overexpenditure of Appropriations

Section 59-701.2 of R.C.M. 1947 provides that "Any just claims not paid

within the fiscal year shall become payable from the succeeding year's appropriation, providing, however, that such claims shall not exceed the appropriation made for the preceding biennium". (Emphasis added). As shown by Exhibits B and C, the Childrens' Center expended or encumbered all but $6 of its General Fund appropriations during the 1965-67 biennium. During the first few months of 1967-68, the agency expended at least $7,345 from its 1967-68 General Fund appropriations in payment for goods and services applicable to the preceding year. Since the appropriations for the 1965-67 biennium had been fully expended, excepting $6, the $7,345 of expenditures were made in direct contrast to the above quoted section.

It might be argued that such expenditures would be offset by similar expenditures incurred during the first few months of the 1965-67 biennium that were applicable to the 1963-65 biennium resulting in expenditures applicable to 1965-67 not exceeding appropriated amounts. Such is not the case, however, as an analysis of expenditures during early 1965-66 shows expenditures totaling $6,435 applicable to 1964-65. The net result even with this argument is that the appropriations were overexpended contrary to the above referenced law.

The prevalance of the above situation throughout the state agencies of Montana is unknown to us since this is the first complete audit examination of a state agency by this office. It would seem that the situation would tend to exist whenever a growing or new state agency runs close to fully expending (on the cash basis) or encumbering its appropriations.

The only logical solution to retain the provisions and intent of the above referenced law appears to be to adopt the "modified accrual basis" of accounting for state operations. This method is the generally accepted basis of accounting for governmental units. Under this system, expenditures are recorded in the year in which they are incurred, as opposed to the year in which they are paid.

RECOMMENDATION

We recommend that the modified accrual basis of accounting be adopted for the State of Montana in order to properly account for expenditures in the year incurred and to avoid the overexpenditure of appropriations.

Overexpenditure of Personal Services Appropriation

During the 1965-66 fiscal year, personal services costs totaling $3,946 were incorrectly charged to the Childrens' Center appropriation for operation and capital. This occurred due to incorrect coding of claims by agency personnel which were not caught by the State Controller's staff in their review prior to disbursement. This resulted in a carryover of $7,043 from the 1965-66 personal services appropriation into 1966-67. The agency's 1966-67 appropriation for personal services ($282,717) plus the $7,043 carryover were recorded as being fully expended during 1966-67 in the State Controller's accounts. Two smaller amounts ($452 in 1965-66 and $432 in 1966-67) for operation were incorrectly charged to the Center's personal services appropriation. The net result is that the Childrens' Center personal services appropriation for the 1965-67 biennium was overexpended by $3,062 due to charging incorrect appropriations.

This situation illustrates the need for revised accounting procedures and improvement of controls exercised by the State Controller's office. The Controller has the responsibility for determining that the proper appropriations are charged.

We suggest that the Controller consider the feasibility of programming the computer in such a way that program expenditures for personal services will be accepted only if charged against an appropriation for personal services. Such a program may not be feasible for all fund appropriations but probably would be for the General Fund.

The implementation of a centralized payroll should serve as an added control over potential incorrect codings.

RECOMMENDATION

We recommend that the State Controller re-evaluate existing controls over appropriation accounting and implement improvements to insure maintenance of a high level of control.

Year-End Purchases

General Fund outstanding encumbrances at June 30, 1967, amounted to $21,419 and consisted primarily of capital equipment items ordered during May and June, 1967. Of the equipment items ordered, $6,400 was for equipment that had been approved for purchase in the 1967-68 fiscal year. This large scale year-end encumbrance of funds resulted in all but $6 of the Childrens' Center 1965-67 biennial appropriation from the General Fund being expended.

The Budget Act (House Bill 526, Section 2) specifically states that "It is unlawful to purchase supplies for a succeeding biennium from an appropriation contained in this act without the approval of the Budget Director". No approvals from the Budget Director were obtained or even sought. In summary, no attempt has been made to comply with this Budget Act provision.

The Budget Director, under Section 79-1018, R.C.M. of 1947 is granted the "power to demand and receive" any information he might need in order to fulfill his duties. We believe that the Budget Director should become involved in the control and review of the appropriations in addition to the preparation and presentation of the Governor's Budget.

The State Controller, under Sections 82-109 through 110, R.C.M. 1947,

is charged with the responsibility for establishing a system of financial control to adequately fulfill his duties. We believe the State Controller and the Budget Director should devise and implement a plan that will result in compliance with the above quoted section of the Budget Act.

An example of such a plan could be: (1) Having a cutoff date (May 15 for example) for the submission of regular requisitions. Requisitions submitted after that date would have to be of an emergency nature and be appropriately justified, and (2) Requiring that all requisitions for equipment items be channelled through the Budget Director's office for approval.

In our opinion the State Controller is obligated to make every attempt possible to comply with this law and the Budget Director should be integrally involved in this control process.

RECOMMENDATION

We recommend that the State Controller and the State Budget Director initiate a plan that will result in compliance with provisions of the Budget Act restricting purchases of subsequent year goods and services from current biennium appropriations at the close of the current biennium.

Erroneous Justification in Support of Budget Requests for Equipment

In the course of our examination of equipment purchases, we compared the list of equipment items actually purchased to the budget requests submitted by the Center through the Office of the Budget Director to the Legislature for the 1965-67 biennium and also for the 1967-69 biennium.

We found that in some cases the agency submitted a request for an equipment item in the second biennium that had been budgeted for and purchased in

the preceding biennium with a similar justification supporting both requests.

The following are two examples for illustration:

Equipment Item Requested	N-R	Cost	Justification	Date Purchased
#1				
1965-66				
Lawn and Garden Tractor	N	$853	With close to five (5) acres of lawn, the present equipment will not keep the boys on top of the job that is needed.	July, 1965
1967-68				
Lawn and Garden Tractor	N	$850	With close to five (5) acres of lawn, the present equipment will not keep the boys on top of the job that is needed.	No additional purchase to date.
#2				
1965-66				
Monroe 10-Column Adding Machine, Intermediate Model	N	$375	Only one adequate adding machine in the entire institution. The volume of work deems a second machine necessary.	Oct., 1965
1967-68				
10-Column Adding Machine, Intermediate Model	N	$400	Only one adequate machine in the entire institution. The volume of work deems a second machine necessary.	No additional purchase to date.

As noted in an earlier section of this report, excess operating funds were used primarily for purchasing additional equipment which either had not been budgeted for or had been budgeted for in the succeeding biennium.

The State Budget Director reviews the justifications set forth by the agencies in support of requests for new or replacement items of equipment.

However, he cannot determine, based upon the information currently made available to him, whether an item of equipment that had been previously budgeted for was actually purchased.

We believe that a procedure should be established whereby the Budget Director is currently informed of the purchases of equipment by the agencies. This information could come from the Purchasing Division of the Department of Administration or from the agencies themselves. Consideration might be given to requiring the approval by the Budget Director prior to any purchases of equipment. Any of these procedures should provide the Budget Director with the information needed to better evaluate budget requests and justifications submitted in subsequent years.

The practice of using unexpended operating funds at year end for the purchase of items of equipment that had not been budgeted for or that had been budgeted for in the succeeding biennium could be controlled by breaking down appropriations into three categories, i.e. personal services, operating expenses, and equipment. Excess operating funds could not then be used for purchasing additional items of equipment.

RECOMMENDATION

We recommend that procedures be established to control and document purchases of equipment to assure compliance with the provisions of the Budget Act.

CONCLUSION

This audit report represents the first report of the Legislative Auditor upon the financial statements of a Montana state agency. The findings have varying degrees of implication and implementation of the recommendations cannot all be adopted by the Childrens' Center directly. In some instances

institution-wide changes should be made which would appropriately be initiated by the Department of Institutions. Other recommendations would require initiation by the State Controller or other control agencies. Finally, revision of certain statutes would be required in some instances such as for the adoption of the modified accrual basis of accounting.

As the reader of this report might gather, this examination of the accounts of one of the smaller Montana state agencies has resulted in a report covering much more than just the operations of the Montana Childrens' Center. Too many confrontations with situations contrary to legal provisions and basic accounting principles were encountered which have a statewide implication to limit our comments to items which the Childrens' Center alone can correct. In several of these areas, the Childrens' Center has acted based upon past experience and knowledge of what is being done in other state agencies.

It might be argued that our comments in this report are premature as to their statewide application where so indicated because this is our first examination of a state agency's financial statements. We would not concur, however, as our comments are also based upon the results of discussions with most of the fiscal officials of state control agencies and upon the findings from our previous review of the system of internal control within the fiscal control agencies.

We wish to express our appreciation to the State officials and employees with whom we worked for their excellent cooperation. We especially acknowledge the fine cooperation of the superintendent of the Childrens' Center and his employees.

Respectfully submitted,

Morris L. Brusett

MORRIS L. BRUSETT
Legislative Auditor

May 2, 1968

EXHIBIT A

MONTANA CHILDRENS' CENTER
BALANCE SHEET
ALL FUNDS
June 30, 1967

	General Fund	Federal and Private Revenue Fund	Bond Proceeds and Insurance Clearance Fund	Agency Fund	General Fixed Assets
Assets					
Cash:					
On Hand	$ 200	$ -	$ -	$ -	$ -
In Bank	1,456	-	-	9,386	-
In State Treasury	-	10,637	-	5,197	-
U. S. Savings Bonds Held in Trust	-	-	-	3,188	-
Due from Other Funds	287	-	-	-	-
Deferred Charges	557	-	-	-	-
Encumbered Appropriation	21,419	-	43,497	-	-
Fixed Assets:					
Land	-	-	-	-	4,271
Buildings	-	-	-	-	1,688,019
Improvements Other than Buildings	-	-	-	-	66,644
Equipment	-	-	-	-	288,515
Total Assets	$23,919	$10,637	$43,497	$17,771	$2,047,449
Liabilities, Reserves, and Fund Balance					
Due to Other Funds	$ -	$ -	$ -	$ 287	$ -
Reserves for:					
Encumbrances	21,419	-	43,497	-	-
Investment in General Fixed Assets	-	-	-	-	2,047,449
Revolving Fund Advance	2,500	-	-	-	-
Fund Balance - Exhibit B	-	10,637	-	17,484	-
Total Liabilities, Reserves, and Fund Balance	$23,919	$10,637	$43,497	$17,771	$2,047,449

MONTANA CHILDRENS' CENTER
STATEMENT OF CHANGES IN FUND BALANCE
ALL FUNDS
Fiscal Year Ended June 30, 1967

	General Fund	Federal and Private Revenue Fund	Bond Proceeds and Insurance Clearance Fund	Agency Fund
Fund Balance, July 1, 1966	$ -	$ 4,442	$ 15,225	$25,544
Additions:				
Appropriations:				
1966-67	491,187	-	-	-
1965-66 Carryover	7,132	-	-	-
Reserve for Encumbrances, July 1, 1966	3,844	-	136,516	-
Revenues	-	9,332	-	16,300
Total Balance and Additions	502,163	13,774	151,741	41,844
Deductions:				
Expenditures:				
Exhibit C	480,738	-	-	-
Exhibit D	-	3,137	-	-
Exhibit E	-	-	108,244	-
Exhibit F	-	-	-	24,300
Reserve for Encumbrances, June 30, 1967	21,419	-	43,497	-
Appropriation Reversion	6	-	-	-
Fund Balance, June 30, 1967	$ -	$10,637	$ -	$17,484

EXHIBIT C

MONTANA CHILDRENS' CENTER
GENERAL FUND
STATEMENT OF EXPENDITURES AND ENCUMBRANCES COMPARED WITH APPROPRIATIONS
Fiscal Year Ended June 30, 1967

	Balance From 1965-66 Appropriation	1966-67 Appropriation	Total Available	Expenditures	Encumbrances	Under (Over) Anticipated
ADMINISTRATION						
Personal Services	$ 150	$ 27,032	$ 27,182	$ 26,935	$ -	$ 247
Operation	-	7,501	7,501	8,751	-	(1,250)
Capital	-	790	790	2,672	2,992	(4,874)
Total	150	35,323	35,473	38,358	2,992	(5,877)
CARE AND CUSTODY						
Personal Services	(258)	164,560	164,302	164,232	-	70
Operation	1,927	132,281	134,208	125,654	1,502	7,052
Capital	-	-	-	-	117	(117)
Total	1,669	296,841	298,510	289,886	1,619	7,005
GENERAL SERVICES AND PHYSICAL PLANT						
Personal Services	5,939	47,048	52,987	52,400	-	587
Operation	2,006	50,789	52,795	41,821	4,445	6,529
Capital	-	8,270	8,270	8,568	9,992	(10,290)
Total	7,945	106,107	114,052	102,789	14,437	(3,174)
EDUCATION AND REHABILITATION						
Personal Services	1,212	44,077	45,289	45,761	-	(472)
Operation	-	9,560	9,560	8,342	269	949
Capital	-	2,000	2,000	6,886	2,102	(6,988)
Total	1,212	55,637	56,849	60,989	2,371	(6,511)
TOTAL - ALL PROGRAMS						
Personal Services	7,043	282,717	289,760	289,328	-	432
Operation	3,933	200,131	204,064	184,568	6,216	13,280
Capital	-	11,060	11,060	18,126	15,203	(22,269)
Sub-Total	10,976	493,908	504,884	492,022	21,419	(8,557)
Less Non-General Fund:						
Federal and Private Revenue Fund	-	2,721	2,721	3,137	-	416
Agency Fund	-	-	-	8,147	-	8,147
NET - GENERAL FUND	$10,976	$491,187	$502,163	$480,738	$21,419	$ 6

MONTANA CHILDRENS' CENTER
FEDERAL AND PRIVATE REVENUE FUND
STATEMENT OF CHANGES IN FUND BALANCE
Fiscal Year Ended June 30, 1967

	Bequest for Construction	Special Milk Program	Land Grant Account	Sewage Lagoon Account	Total
Fund Balance, July 1, 1966	$ -	$3,509	$522	$411	$ 4,442
Receipts:					
Reimbursements from Federal Government	-	3,113	-	-	3,113
Proceeds from Estate Bequest	6,219	-	-	-	6,219
Total Balance and Receipts	6,219	6,622	522	411	13,774
Disbursements:					
Milk Purchases, Milk Dispensers and Stands, Paper Cups, etc.	-	2,999	-	-	2,999
Land Discing	-	-	50	-	50
Construct Cattleguard and Abutment	-	-	-	88	88
Fund Balance, June 30, 1967	$6,219	$3,623	$472	$323	$10,637

EXHIBIT E

MONTANA CHILDRENS' CENTER
BOND PROCEEDS AND INSURANCE CLEARANCE FUND
STATEMENT OF EXPENDITURES AND ENCUMBRANCES COMPARED WITH APPROPRIATIONS
Biennium Ended June 30, 1967

Project	Appropriation	Inter-Project Transfers	Expenditures 1965-66	Expenditures 1966-67	Encumbrances	Unencumbered Balance
Repair, Renovate, Reroof Cottages and Gymnasium and Provide New Water Supply System	$130,000	$ 16,474	$ 484	$102,493	$43,497	$ -
Repair Water Tank	7,000	(1,249)	-	5,751	-	-
New Boiler	55,000	(15,225)	39,775	-	-	-
Total	$192,000	$ -	$40,259	$108,244	$43,497	$ -

MONTANA CHILDRENS' CENTER
AGENCY FUND
STATEMENT OF CHANGES IN FUND BALANCE
Fiscal Year Ended June 30, 1967

	BEQUESTS FOR				
	Recreational Purposes	Buildings and Equipment	General Use	Childrens' Trust Accounts	Total
Fund Balance, July 1, 1966	$5,796	$ 727	$5,321	$13,700	$25,544
Receipts:					
Dividend Income	-	282	-	-	282
Deposits to Childrens' Accounts	-	-	-	16,018	16,018
Total Balance and Receipts	5,796	1,009	5,321	29,718	41,844
Disbursements:					
Recreation and School Equipment and Supplies	5,852	-	2,295	-	8,147
Withdrawals from Childrens' Accounts	-	-	-	16,213	16,213
Fund Balance, June 30, 1967	$ (56)	$1,009	$3,026	$13,505	$17,484

MONTANA CHILDRENS' CENTER
STATEMENT OF CHANGES IN GENERAL FIXED ASSETS
Fiscal Year Ended June 30, 1967

	Land	Buildings	Improvements	Equipment	Total
Balance, July 1, 1966	$4,271	$1,688,019	$66,644	$217,293	$1,976,227
Additions:					
Expenditures for Capital Items During 1965-66	-	-	-	57,646	57,646
Expenditures for Capital Items During 1966-67	-	-	-	18,126	18,126
Total Balance and Additions	4,271	1,688,019	66,644	293,065	2,051,999
Deductions:					
Write-offs for Items Traded-In, Lost, Worn Out, Etc. During 1965-66	-	-	-	4,550	4,550
Balance, June 30, 1967	$4,271	$1,688,019	$66,644	$288,515	$2,047,449